BEFORE THE

PUBLIC SERVICE COMMISSION OF WISCONSIN

Application of Wisconsin Public Service Corporation for Authority to Adjust Electric and Natural Gas Rates	))	6690-UR-124

Rebuttal Testimony
of
Rick J. Moras
for
Wisconsin Public Service Corporation

September 21, 2015

Q. Please state your name, business address and position.

A. My name is Rick J. Moras. My business address is WEC Energy Group, Inc. ("WEC"), 700 North Adams Street, P.O. Box 19001, Green Bay, WI 54307-9001. I am the Director of Operations Accounting for Wisconsin Public Service Corporation ("WPSC"). I am testifying on behalf of WPSC in support of its application in this proceeding for authority to adjust its electric and natural gas rates.

Q. Please describe your educational, professional, and utility background.

A. I graduated from Michigan Technological University in 1977 with a Bachelor of Science degree in Accounting. My professional designations are Certified Public Accountant and Certified Internal Auditor. I have been employed by WPSC since 1980, and have held various positions in the Accounting and Finance organization over that time. In my current position, I am responsible for operational finance and accounting for WPSC. I have previously testified before the Commission on issues related to Wisconsin Fuel and Light Company merger synergy savings, and various revenue requirement issues in WPSC's rate cases.

Q. What is the purpose of your rebuttal testimony?

A. The purpose of my rebuttal testimony is twofold. First, I identify those non-fuel Operation and Maintenance ("O&M") and net investment rate base adjustments proposed by Staff witness Ms. Kettle in her direct testimony that WPSC accepts. Second, I identify and discuss those non-fuel adjustments proposed by Ms. Kettle that WPSC believes are unreasonable, either in whole or in part: Adjustment Nos. 9, 10, 11 15, 18, 19, 22, 23, 26, 27, 31, 32, 34, 35, and 36. The dollar amounts in my rebuttal testimony are on a corporate basis.

In addition to these non-fuel O&M adjustments, WPSC believes that Ms. Kettle's recommended adjustments to net investment rate base for ReACT and other construction expenditures, as described by Ms. Kettle on page 24 of her direct testimony, are not reasonable.

Q. Please identity the adjustments proposed by Ms. Kettle that WPSC accepts.

A. WPSC accepts the following non-fuel O&M adjustments proposed by Ms. Kettle: Adjustment Nos.12, 13, 14, 16, 17, 20, 21, 24, 25, 28, 29, 30, and 33. In addition, WPSC does not oppose Ms. Kettle's adjustments to net investment rate base for Fox 3, construction expenditures not related to in-service, retirements, electric fuel inventory, customer advances, and gas in storage.

Q. Please describe Exhibit Ex.-WPSC-Moras-2.

A. This exhibit summarizes Staff's non-fuel O&M adjustments, indicates WPSC's position on each, and provides the revenue requirement impact of reversing the adjustments that WPSC opposes in whole or in part as I discuss below.

Q. Why does WPSC oppose Staff's proposed reduction of non-union labor expense by $1.2 million (Adjustment No. 9)?

A. WPSC opposes this adjustment because it assumes that the company will have <u>zero</u> non-union wage escalation in 2016. This assumption is false. In March 2015 a 2.6% wage increase was given to non-union employees. That wage increase should be recognized in WPSC's 2016 rates and the $1.2 million adjustment should be rejected in its entirety.

Q. Why does WPSC oppose Staff's various proposed adjustments relating to non-executive incentive compensation totaling $7.516 million?

A. WPSC's total compensation of non-executive employees -- estimated in 2016 to be $177.469 million -- is targeted at a mid-market level as determined by our compensation consultant. Staff has not challenged the reasonableness of setting total compensation at that level. Rather, Staff proposes the disallowance of the portion of total non-executive compensation that is "at risk" and paid out (or not) subject to WPSC's non-executive incentive compensation program. As described by Ms. Hinkes, this program establishes incentives for employees that are aligned with customer interests. Questioning the need and efficacy of these incentives, Staff proposes to disallow recovery the entire amount ($7.516 million) of WPSC's 2016 non-executive "at risk" payroll expense.

Given the reasonableness of WPSC's median market-based total compensation of its non-executive employees and the reasonableness of the incentives governing payment of the "at risk" portion of that total, the Commission should reject Staff's proposed adjustments in their entirety and restore $7.516 million to the company's 2016 revenue requirement.

Q. Why does WPSC oppose Staff's proposed reduction of $718,000 in third party storm assistance costs (Adjustment No. 15)?

A. The 3-year average (2012-2014) that Staff used is not appropriate because of the wide variation of weather patterns and resulting costs in recent years. The variation in costs over these 3 years is as follows:

2012	$43,000
2013	$79,000
2014	$650,000

The variability of the 3-year average is moderated if 2011 ($969,000) is included. WPSC would accept the use of a 4-year average for these costs, which would reduce the Staff adjustment by $178,000.

Q. What is WPSC's position on Staff Adjustment No. 18, which removes $1,166,000 associated with the purchase of station power service for Fox Energy Center from Kaukauna Utilities?

A. WPSC agrees that its 2016 rates should reflect that it will be self-serving station power to the Fox Energy Center, so this adjustment is appropriate. However, the company's fuel forecast should reflect the cost of fuel WPSC will incur to self-serve this station power. The estimate of this cost -- $190,000 -- is supported by Mr. Guntlisbergen’s rebuttal testimony and should be added to the company's revenue requirement.

Q. Why does WPSC oppose Staff's proposed 25% reduction of bad debt expense for delays in the collection process due to the implementation of ICE (Adjustment No. 19)?

A. This adjustment, which comprises $1.45 million of Staff's total adjustment to uncollectible expense of $1.74 million, is not appropriate. The adjustment erroneously assumes that delays in WPSC's collection process caused by the implementation of ICE will result in a reduction in amount of accounts written off during 2016. This is not correct. Although there will be delays in the write-off process, they will not reduce the amount of write-offs WPSC will experience in the test year.

Ms. Kettle bases her 25% adjustment to uncollectible expense based on three delays in WPSC's collection process resulting from the implementation of ICE that will total 81 days, or about 25% of the year. However, none of these delays will result in any reduction in WPSC's uncollectible expense.

The first delay is a 30-day delay in recording write-offs after ICE is implemented. This delay will not, however, eliminate a months' worth of write-offs as Staff assumes. The delay will occur in the 4th quarter of 2015. The write offs that would be done in December 2015 will be shifted into January 2016, the write offs that would be done in January 2016 will be shifted into February 2016, and so forth. Thus, WPSC will have 12 months of actual write-offs in 2016.

The other delays are two 21-day "credit delays," one before and one after ICE implementation. During these periods there will be no residential disconnection notices issued or disconnections taking place. These delays will not impact residential bad debt expense because the implementation of ICE will occur in the fourth quarter during the 2015 winter moratorium when no residential disconnections are taking place anyway.

The only potential impact related to the ICE-related delays would be to commercial collections, which should be minimal.

- In 2013 the WPSC total bad debt was $5,247,013 of which commercial contributed only $313,195 (6%).
- In 2014 the WPSC total bad debt was $7,338,225 of which commercial contributed only $350,840 (5%).

The effect on commercial collections will be to delay bad debt expense from 2015, which will increase the 2016 test year amount by the amount delayed. Normal credit and collections will resume in December 2015 or January 2016. In any event, the impact on WPSC's total bad debt expense should be minimal.

For all of these reasons, $1,452,000 of Staff's adjustment to uncollectible expense should be restored.

Q. Why does WPSC oppose Staff's proposed reduction of $1,382,000 in outside services related to strategic services (Adjustment 23)?

A. This adjustment should be rejected because it erroneously assumes that WPSC will no longer receive certain "strategic" services as the result of Integrys' acquisition by Wisconsin Electric. Yet these services are and will continue to be provided by in-house specialists employed by WEC Business Services in the areas of benefits, compensation, talent management, project services, tax, regulatory, supply chain, and investor relations. The fact that WPSC's holding company has changed has nothing whatsoever to do with the services the company will continue to need in order to continue to make decisions in the best interest of the company and its customers.

Q. Why does WPSC oppose Staff's proposed reduction of $518,000 in outside services related to Administrative and General ("A&G") credits from American Transmission Company ("ATC") (Adjustment 23)?

A. This adjustment should be rejected because it is based on a unique approach Staff appears to have used in order to maximize the amount of these credits, which are part of the compensation ATC pays WPSC for services. Rather than basing this item on a multi-year average as it does with most revenue requirement components, Staff calculated the average rate of increase of these credits over 3 years and assumed that a similar increase -- 16% -- would occur through 2016. The implication is that the WPSC’s A&G is increasing at approximately the same rate of 16%, which is not the case. A 3-year or 4-year average of the actual credit amounts would adequately capture "the increasing trend for this item." Accordingly, $448,000 to $490,000 of Staff's adjustment should be restored to the company's revenue requirement.

Q. Why does WPSC oppose Staff's proposed reduction of $886,000 in costs related to injuries and damages (Adjustment 26)?

A. This adjustment should be partially restored to reflect a more reasonable historical average of these costs. Rejecting WPSC's forecast, Staff used a 3-year average (2012-2014) of actual costs. This average included a year (2013) in which WPSC had an unusually large credit (over $500,000) in this area due to a recovery against a co-defendant. Because of the wide variation of injuries and damages claims each year, a 4-year average of historical costs would be more reasonable. Based on a 4-year average, $394,000 of this adjustment should be restored to the company's revenue requirement.

Q. Why does WPSC oppose Staff's proposed reduction of the company's forecast of active medical expense by $3,699,000 (Adjustment 27)?

A. This adjustment should be partially restored -- by $2,648,000 -- to more accurately reflect the trend of actual expenditures of this nature. Staff compared the company's forecasted and actual expenses in the years 2009, 2011, 2013, and 2014, and assumed that a similar difference would occur in 2016. The adjustment is quite large and represents a reduction in WPSC's forecast by 18%. WPSC analyzed the trend of these costs in the years 2013 through June 2015. This analysis, which is based on more recent data than Staff's purely historical look back to <u>2009</u>, results in a modified forecast of $19,777,000, which is $1,051,000 less than its filed forecast amount without inflation. WPSC would accept an adjustment in this amount to its filed amount, which would require $2,648,000 of the Staff adjustment to be restored.

Q. Why does WPSC oppose Staff's proposed reduction of $3,800,000 to employee payroll and benefits to eliminate the wages, benefits, and payroll taxes for those Integrys employees who were subject to change in control terminations as the result of Wisconsin Energy's acquisition of Integrys (Adjustments 9 and 27)?

A. There is absolutely no basis for this adjustment, which assumes that WPSC will operate in 2016 without any senior executive leadership. Although the Integrys employees who were subject to change in control terminations are no longer employed by the combined company, and no portion of <u>their</u> costs will be allocated to the company in 2016, WPSC will continue to receive leadership and direction from the senior executives of WEC Energy Group and will be allocated costs accordingly. The amount of these costs contained in WPSC's proposed revenue requirement is a reasonable estimate.

Further, a portion of this adjustment -- $836,000 -- erroneously assumes that an accounting termination of non-qualified pension plans of the terminated Integrys executives, and an acceleration of the related expense, occurred in <u>2015</u> as a result of the acquisition. This is simply untrue. The cost recognition of Integrys non-qualified pension plans follows GAAP accounting under ASC 715-30 (formerly FAS 87). For those terminated Integrys executives who elected to receive lump sum distributions of their pensions, settlement accounting will be triggered and the recognition of the expense of the actuarial losses will be recognized. But under GAAP this will not occur until <u>2016</u> and WPSC has not included these expenses in its 2016 test year. Instead, WPSC's 2016 costs assume normal actuarial assumptions <u>had the acquisition not occurred</u> Excluding this expense in its entirety would deprive WPSC of recovery of a reasonable cost of doing business and deviate from past practice of allowing actuarially calculated expense under ASC 715-30.

For these reasons, this adjustment should be rejected in its entirety.

Q. Why does WPSC oppose Staff's proposed elimination of $787,000 in costs charged for the Integrys Board of Directors (Adjustment 31)?

A. Like the previous adjustment, this adjustment erroneously assumes that there will be no replacement of the oversight of WPSC and the related costs. Although the Integrys board was obviously eliminated as a result of the acquisition, WPSC will continue be lead and directed by its corporate parent and its board, and of course allocated a portion of the costs of the WEC Energy Group board.

It is beyond dispute that effective board oversight is an essential and necessary business function to ensure an efficiently well-run organization. Acceptance of Staff's proposed adjustment would create a known revenue shortfall for a legitimate business-related cost that no one denies is appropriate and will occur.

Staff nonetheless contends that WPSC should be denied this legitimate business expense because the cost of the former Wisconsin Energy board is being recovered from WEPCO and WG. Staff's contention is unfounded for several reasons. First, it is not true that the full cost of the <u>WEC Energy Group</u> board will be fully recovered from WEPCO and WG in 2016 because that board has 3 additional members and the scope of its responsibilities has increased as a result of the acquisition. Second, the mix of actual costs incurred by WEPCO and WG relative to what was allowed in past rate cases changes over time—some go up and some go down—and they strive to manage overall total costs between rate cases to have an opportunity to earn their authorized returns. By definition, Staff's contention that WEPCO and WG will necessarily recover all of the costs included in their last approved revenue requirements cannot be proven. Third, WEPCO and WG are expected to have their revenue requirements adjusted across the board—including their allocated board of directors expense—in a test year 2017 rate case, whereas WPSC isn't likely to have its revenue requirement adjusted again until 2018. Finally, if and to the extent that the allocation of holding company board costs to WPSC were to cause or contribute to overearnings by WEPCO and/or WG, the overearnings would be shared with customers under the earnings sharing mechanism provided in the order approving Wisconsin Energy's acquisition of Integrys.

In short, holding company board of directors expenses are legitimate costs of service for WPSC in this rate case regardless of how the rates of other WEC Energy Group utilities were set in the past. This adjustment should be rejected in its entirety.

Q. Why does WPSC oppose Staff's proposed elimination of $170,000 in membership dues for EPRI (Adjustment 32)?

A. In prior rate cases, the Commission has recognized the value of EPRI research to WPSC customers and has allowed the company to recover 100% of its EPRI dues. Staff offers no basis to change this policy and 50% of the EPRI dues ($170,000) should be restored to the company's revenue requirement.

Q. What is WPSC's position on Staff's proposed reduction of non-labor O&M expense inflation by almost $4 million for 2015 and 2016 (Adjustments 22 and 34)?

A. WPSC agrees that CPI is a reasonable basis for escalation of non-labor O&M expense, but Staff has not documented it assumption of <u>zero</u> CPI inflation for 2015. Based on the July 2015 CPI forecast from Moody's Analytics, inflation will be 0.40% in 2015 and 2.66% in 2016. WPSC would accept the application of these objective forecasts, which would restore $773,000 ($29,000 to Adjustment 22 and $744,000 to Adjustment 34) of these adjustments to the company's revenue requirement.

Q. What is WPSC's position on Staff's proposed adjustment to taxes other than income taxes (Adjustment 36)?

A. There is an error in Staff's calculation of this adjustment. Staff included both WPSC and IBS-allocated wages in the calculation, but only WPSC FICA expense. Including the IBS-allocated FICA expense in the calculation would reduce the adjustment by $361,000. In other words, the net adjustment would go from a reduction of $15,000 to an increase of $346,000.

Q. Why does WPSC oppose Staff's proposed reduction of net investment rate base by $4,782,000 to reflect slower construction closings and increased CWIP balances (Adjustments 35b and Cc)?

A. Staff's adjustment is based on a faulty methodology and should be rejected in its entirety. Instead of accepting WPSC's forecasts for 2016, Staff used a concoction of historical data on the completion of construction projects ("closings") from 2011 and 2012, as well as forecasted closings in 2014, to reduce the number of forecasted closings in 2015 and 2016. This has the effect of increasing WPSC's CWIP balances during the test year and decreasing its depreciation expense and increasing associated AFUDC.

As shown in Exhibit Ex.-WPSC-Moras-3, the CWIP balances for 2016 that result from Staff's methodology are grossly overstated. Staff's "forecasted" total CWIP balance (excluding generating assets) at its peak in 2016 is $26.2M or 47% higher than the highest level of WPSC's actual CWIP ($55.9M in September 2014) since January 2013 or forecasted through 2016. Specifically, Staff's 2016 CWIP balance related to Plant Account 367 Distribution Plant-Underground Conductor and Devices is $36.4M or 154% higher than the $23.7M CWIP balance in September 2014. Account 391 General Plant-Office Furniture and Equipment has a $1.9M CWIP balance in 2016 when typically WPSC has no CWIP balance. Account 392 General Plant-Transportation Equipment has a 2016 CWIP balance over $1.5M higher than September 2014, an increase of 68%.

Staff's methodology can only be described as a results-driven approach to reduce WPSC's revenue requirement, and the adjustment should be rejected in its entirety. However, if the Commission does not reject this adjustment, then a correction needs to be made. In making its adjustment, Staff imputed AFUDC on the construction involved. However, revenue requirements did not reflect the additional AFUDC in rate base, or the tax effect of the debt AFUDC which reduces interest expense. As a result revenue requirements are understated $200,000 and $160,000, respectively, and these amounts should be restored to the company's revenue requirement.

Q. What is WPSC's position on Staff's proposed adjustment of $70M to plant in service related to the ReACT project?

A. WPSC does not oppose this adjustment, provided that a deferral is allowed for the difference between the assumed and actual associated revenue requirement in 2016, with the revenue requirement including the carrying cost of plant not recovered at the weighted cost of capital and the related depreciation expense. This is the treatment the Commission allowed for WPSC's Fox Energy Center purchase in 2013. The deferral would be reviewed in the next filed WPSC rate case.

Q. Should the Commission consider additional adjustments to payroll to reflect synergy savings in the test year associated with Wisconsin Energy's acquisition of Integrys?

A. No. WEC Energy Group has described the compelling reasons for the acquisition were the creation of a larger Wisconsin-based company with greater financial liquidity, flexibility, and improved access to capital markets, including the ability to use the strong cash flow of the combined companies to fund future investments without issuing new debt. The company has also stated that it expects the opportunity for increased efficiencies in operations, purchasing, and corporate services to occur over time. The company committed to not reducing its represented labor force beyond normal attrition for two years following the closing of the transaction, which became order point 25 in the order approving the acquisition in docket 9400-YO-100. The company also agreed that no transaction costs incurred by or allocated to WEPCO, WG, and WPSC would be recovered from customers, and that WEPCO and WG will be subject to an earnings sharing mechanism for three years beginning in 2016. In addition, any transition costs will not be recovered from customers until the company shows that the benefits are greater than the costs to achieve them. As discussed in the acquisition order, the earnings sharing mechanism will ensure that, to the extent benefits in the form of synergy savings are realized in excess of the costs to achieve them, and the company earns at least its authorized return, the savings will be shared with ratepayers. Given these commitments that are reflected in the acquisition order, it would not be appropriate for the Commission to impute a payroll synergy savings adjustment in this proceeding.

Q. Does this complete your rebuttal testimony?

A. Yes, it does.